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Ms. Marlene H. Dortch
Secretary,
Federal Communications Commission
445 Twelfth Street
Washington, D.C. 20554

Re: Ex Parte Presentation, CC Docket No. 96-45

Pursuant to Section 1.1206 of the Commission's rules, Valor Telecommunications of Texas, L.P. ("Valor") supplements the record in the above-referenced docket with regard to its *Petition for Waiver of Section 54.305* filed on April 11, 2003 ("Parent Trap Waiver").

Background: Valor acquired rural exchanges from GTE in 2000, and began operating in Texas in the third quarter of 2000. Valor's high-cost support is capped by the Parent Trap rule, 47 C.F.R. § 54.305, limiting its total support to the amount received by GTE pre-acquisition. In 2000 and 2001, Valor was forced to expend substantial capital investments into its network due to the overall condition of the acquired network; unexpected capital and expense costs to repair damage caused by natural disasters (ice storms); and one-time expenses directly related to the acquisition. As a result, Valor expended far greater amounts of capital expenditures in those years than in a "normal" year of operations.

In May 2001, after Valor had acquired the Texas study area and in the midst of Valor's efforts to overcome these challenges, the Commission adopted the safety valve rule, a backstop mechanism intended to somewhat ameliorate the adverse effects of the Parent Trap rule. The impetus for the reform, according to the Rural Task Force, was that "high-cost exchanges should not be 'doomed' to poor service because the selling carrier has limited access to universal service support funds." *Rural Task Force Order,* ¶ 93. In adopting the reforms, the Commission explicitly recognized that the Parent Trap rule "may have some unintended consequences." *Id.,* ¶ 97.

As you know, safety valve support is based on the difference between "index year" expenses and expenses in subsequent years. Under the rule, the "index year" is the first full year of operations after the acquisition. Rural carriers only receive support under the rule based on fifty percent of the amount of investments in later years that exceeds the investments made in the index year.

This arbitrariness of the timing (the reform occurred after the affected transaction) has prevented the safety valve rule from serving its intended purpose for Valor. *See Parent Trap Waiver at fn. 6.* Because 2001 is Valor's "index year" (a year of exceedingly high capital expenditures and related network operations costs), Valor is essentially foreclosed from receiving safety valve support in meaningful amounts. As a result, the rule does not provide Valor support that "reasonably approximates [Valor's] new investments in the acquired exchanges." *Rural Task Force Order,* ¶ 101. Moreover, Valor is forced to operate pursuant to a rule that did not exist at the time of the affected transaction.

If the rule had been in effect, Valor may have been able to time investments so that the rule would produce some benefits. Setting aside the clear public interest problems with a decision to delay needed investments, the result is manifestly inconsistent with Section 254's mandate that universal service be sufficient and predictable. Moreover, to the extent the safety valve rule is intended to "provide acquiring carriers with predictability," it failed woefully for Valor. *Rural Task Force Order,* ¶ 100. As a result, the FCC's rules have prevented Valor from receiving sufficient high-cost support. In fact, Valor receives far less than similarly-situated rural carriers.

Waiver Request: To remedy this shortfall, Valor proposed a waiver of Parent Trap rule this April, consistent with pre-safety valve rule precedent, so as to allow Valor to received support based upon actual Texas loop costs, thereby placing Valor on an equal footing with other rural carriers. Valor maintains that the Parent Trap rule would be the most reasonable approach in light of the peculiar circumstances affecting Valor.

Alternative Approach: Absent a Parent Trap waiver, however, it would be possible to produce meaningful universal service support to Valor under the current rules by granting a waiver that would only slightly modify the safety vale rule's index year. As described above, the current index year, 2001, is artificially inflated due to the substantial capital expenditures that Valor made in Texas during 2001 in order to meet customer expectations and service quality standards mandated by the Texas Public Utilities Commission. The purpose of the index year is to serve as a baseline measuring stick to evaluate whether expenditures in subsequent years have increased. An idiosyncratic index year dooms any such evaluation. Valor proposes to strip away the one-time and unexpected expenditures from its initial expenses to develop a true baseline index year with which to evaluate future years

Administratively, modifying Valor's annualized expenses for 2000 is a more transparent and simpler process than modifying the 2001 expenses. This is because the four months in 2000 following the close of the transaction are cleaner for analysis purposes. Valor has developed its "index year" by segregating those expenses relating to anomalous events (ice storms, one-time acquisition expenses) that can be isolated. Valor input adjustments to the necessary NECA data lines to derive an adjusted loop cost per Part 36 rules. Making the adjustments to the prescribed algorithm produces an adjusted 2000 loop cost of $306.15.

In order to develop the adjusted 2000 loop cost, Valor used the following methodology:

- The starting point was Valor's annualized 2000 results, as reflected in Valor's 2001 492 filing. In that filing, the FCC accepted Valor's four months of 2000 operations on an annualized basis for purposes of calculating the low-end formula adjustment mechanism ("LFAM") under the price cap rules.
- The following adjustments were made to the annualized operating results:

    - One-time costs related to the start-up of Valor's operations in Texas were removed. These costs were associated with such items as network operations, data conversion and implementation of new systems.
    - Capital and expense associated with the Texarkana ice storm were removed. Valor incurred $3,250,000 expense and $1,500,000 in capital expenditures in 2000 related to the ice storm.
    - Valor normalized its actual 2000 network operating expenses by removing extraordinary operating costs and expenses directed related to the commencement of Valor's network operations after the acquisition. Valor incurred these additional network operating costs of approximately $6.8 million. Network operating costs include costs such as central office and outside plant personnel, outside contractors and network monitoring that were necessary in order to establish a minimum level of service and to complete the acquisition.

The attached spreadsheet shows the safety valve calculation based on the adjusted loop cost of $306.15. It also shows that even after adjusting the 2000 loop cost as proposed by Valor, the safety valve calculation produces a level of high cost support less than what Valor would qualify for if the Commission waived the Parent Trap rule.

Valor emphasizes that continuing at the current level of support cannot be an option under the requirements of Section 254. Valor's current high-cost support is 'insufficient" for Valor's Texas operations. Without additional support, Valor's rural customer base with be shortchanged, and Valor's ability to effectively serve its customers will be curtailed. Please contact the undersigned with any questions regarding the Parent Trap wavier request or the alternative relief proposed herein.

Respectfully submitted,

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Counsel for Valor Telecommunications of Texas, L.P.

cc: Sharon Weber
Paul Garnett

SAFETY VALVE CALCULATION

Texas		Valor 2000 adj	Valor 2002
Loop Costs		$306.15	$371.17
Working Loops			320,627
Difference in cost	$65.02		
X 50%	$32.510000		
X working loops	$10,423,584		
Monthly Requirement	$868,631.98		
Current 54.305 mthly amt	$71,120.00		
Monthly Total	$939,751.98		
Monthly if 54.305 waiver is granted	$1,112,991.83		
Is Total receipts less than amount Valor would have received w/o 54.305??	YES		